

Message Text

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ACTION EB-07

INFO OCT-01 ISO-00 IO-13 AF-08 ARA-06 EA-07 EUR-12 NEA-10

FEA-01 ERDA-05 AID-05 CEA-01 CIAE-00 CIEP-01 COME-00

DODE-00 FPC-01 H-01 INR-07 INT-05 L-03 NSAE-00 NSC-05

OMB-01 PM-04 OES-06 SP-02 SS-15 STR-04 TRSE-00

ACDA-07 INRE-00 SSO-00 NSCE-00 USIE-00 /138 W

-----201823Z 117945 /42

O R 201740Z JAN 77

FM AMEMBASSY LONDON

TO SECSTATE WASHDC IMMEDIATE 9690

INFO AMEMBASSY ABU DHABI

AMEMBASSY ALGIERS

AMEMBASSY BONN

AMEMBASSY BRASILIA

AMEMBASSY CARACAS

AMEMBASSY DOHA

AMEMBASSY JAKARTA

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AMEMBASSY TOKYO

AMEMBASSY TRIPOLI

AMEMBASSY VIENNA

USMISSION OECD PARIS

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E.O. 11652: GDS

TAGS: ENRG UK OPEC

SUBJECT: BRITISH VIEWS ON OPEC TWO TIER PRICING

REF: 76 LONDON 20869; LONDON 24; LONDON 915

1. SUMMARY: HMG OFFICIALDOM IS ADOPTING A SKEPTICAL VIEW OF SAUDI CHANCES TO WIN A CLEAR CUT VICTORY IN THE TWO TIER PRICING BATTLE. BRITISH OFFICIALS TEND TO BELIEVE THAT THE DYNAMICS OF THE OIL MARKET WILL RESOLVE THE PRICE QUESTION OVER TIME AND THAT THERE IS LITTLE CONSUMER GOVERNMENTS CAN DO TO INFLUENCE THE OUTCOME. THEY ALSO REASON THAT WORLDWIDE ECONOMY RECOVERY MAY INCREASE OIL DEMAND TO A LEVEL WHICH WILL ENABLE THE OPEC ELEVEN TO OUTLAST THE SAUDIS AND MOVE PRICES CLOSER TO THE 10 PERCENT FIGURE AFTER MIDYEAR. THIS SAID, THE BRITISH PROBABLY COULD BE BROUGHT AROUND TO CONSIDERING INITIATIVES DESIGNED TO HELP THE SAUDI-UAE CAUSE IF THEY WERE LOW KEY AND DIDN'T "CONFRONT" ESPECIALLY THE IRANIANS IN TOO DIRECT FASHION. FROM AN INDUSTRY STANDPOINT, SHELL AND ESPECIALLY BP ARE UNHAPPY WITH THEIR COMPETITIVE DISADVANTAGE VIS A VIS THE ARAMCO PARTNERS AND ARE HOPING FOR AN EARLY COMPROMISE WHICH WOULD ELIMINATE TWO TIER PRICING ALTOGETHER. END SUMMARY.

2. IN REACHING THEIR SUMMARY CONCLUSIONS, UK OFFICIALS HAVE EXPRESSED DOUBTS BOTH AS TO THE SAUDI ABILITY TO INCREASE PRODUCTION AS RAPIDLY AS MAY BE REQUIRED TO WIN THEIR POINT AS WELL AS THE ABILITY (OR WILLINGNESS?) OF OIL COMPANIES TO DRAW DOWN STOCKS AT A PACE RAPID ENOUGH TO PLACE STRONG PRESSURE ON THE OPEC ELEVEN. THE BRITISH BELIEVE SOME COMPANIES MAY HEDGE AGAINST THE RISK OF HIGHER PRICES WITHIN THE NEXT FEW MONTHS BY MAINTAINING SUBSTANTIAL INVENTORIES AND CONTINUING TO CONFIDENTIAL

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PURCHASE ON A BUSINESS AS USUAL BASIS. HMG THINKING MAY WELL BE INFLUENCED BY THEIR SYMPATHY FOR BP'S, AND TO A LESSER EXTENT SHELL'S, COMPETITIVE POSITION AND DESIRE TO SAFEGUARD ITS LONGER TERM PREFERRED STATUS IN IRAN. MOREOVER, AS REPORTED REFTEL (LONDON 915), THE UK HOPES TO AVOID ANTAGONIZING IRAN AS ITS LARGEST MIDDLE EAST EXPORT MARKET.

3. THE BRITISH ARE OF COURSE INTENT NONETHELESS ON OBTAINING THEIR FAIR SHARE OF WHATEVER ADDITIONAL SAUDI CRUDE IS MADE AVAILABLE, BOTH FOR BALANCE OF PAYMENTS REASONS AND TO ENSURE THAT UK INDUSTRY SUFFERS NO COMPARATIVE DISADVANTAGE AS A CONSEQUENCE OF HIGHER ENERGY PRICES. BUT THE UK MAY BE CAUTIOUS ABOUT ADOPTING ANY MEASURES SUGGESTED IN THE IEA WHICH ARE DESIGNED TO FACILITATE THE MONITORING OF CHEAP SAUDI/UAE CRUDE IMPORTS. THE UK MIGHT AGREE, HOWEVER, TO ASSUME A LOW PROFILE, FOLLOW THE LEADER APPROACH WHICH IS NOT APT TO ANTAGONIZE THE IRANIANS UNDULY. IN THIS CONTEXT, THE

DEPARTMENT OF ENERGY HAS DENIED A PIW REPORT THAT THE UK IS PREPARED TO FOLLOW A PURPORTED US LEAD ON THE INTRODUCTION OF A CRUDE COST EQUALIZATION SCHEME. IN DOING SO, IT WAS NOTED THE UK WAS AWARE HOWEVER OF FRENCH INTEREST IN SUCH A SCHEME. THE UK ALSO MIGHT BE LOATHE TO AGREE TO A CONCERTED IEA MOVE TO ENCOURAGE A RAPID RUNDOWN IN STOCKS LEVELS, ALLEGEDLY BECAUSE OF A CONCERN THAT SOME OF THE WEAKER LINKS IN THE IEA CHAIN MIGHT NOT REBUILD THEM SUBSEQUENTLY. FURTHER, THE BRITISH MIGHT ARGUE THAT SHARPLY REDUCED STOCK LEVELS WOULD LEAVE IEA CONSUMER COUNTRIES TOO VULNERABLE TO CUTOFF OF OIL IMPORTS IN THE EVENT OF A RENEWED

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ACDA-07 INRE-00 SSO-00 NSCE-00 USIE-00 /138 W
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O R 201740Z JAN 77
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MIDDLE EAST CRISIS. IN SHORT, THE BRITISH CAN BE EXPECTED TO ARGUE TWO TIER PRICING IS NOT LIKELY TO LAST INDEFINITELY, THAT THE SITUATION IS STILL QUITE MUDDLED AND PRECIPITOUS ACTION OUGHT TO BE AVOIDED. (NOTE: THERE IS NO FIRM HMG LINE AS YET ON THESE MATTERS BUT THE TENOR OF OFFICIAL LEVEL COMMENTS IN FCO AND ENERGY DEPARTMENT LEAD US TO THESE CONCLUSIONS ABOUT LIKELY HMG POSTURE.)

4. WITH RESPECT TO SHELL, THE COMPANY IS SMARTING SOMEWHAT OVER ITS COMPETITIVE DISADVANTAGE VIS A VIS THE ARAMCO PARTNERS BUT IS KEEPING ITS COOL. SHELL AGREES THAT KUWAIT, IRAQ AND ESPECIALLY IRAN ARE THE KEY FACTORS IN DETERMINING THE OUTCOME OF THE PRICE BATTLE. THE KUWAITIS ARE SEEN AS POSSIBLY NERVOUS ABOUT BEING AT ODDS POLITICALLY WITH THE SAUDIS, BUT PHYSICALLY CAPABLE OF MAINTAINING SUFFICIENT CRUDE PRODUCTION TO RUN THEIR ASSOCIATED GAS FACILITIES SINCE FAR LESS THAN 1.5 M/B/D IS NEEDED TO RUN THEM DURING THE WINTER MONTHS. ON IRAQ, SHELL AGREES THAT ON THE BASIS OF PAST PERFORMANCE THE IRAQIS SHOULD SOON BEGIN TO CHISEL ON PRICES, BUT AS YET HAS SEEN NO HARD EVIDENCE TO SUPPORT THIS EXPECTATION. THE IRANIANS ARE CITED AS THE NUB OF THE PROBLEM AND TOUGH TALKS INVOLVING THE CONSORTIUM ARE EXPECTED.

5. SHELL DISCOUNTS MANY OF THE RUMORS HEARD ABOUT POSSIBLE MEETINGS IN THE NEAR FUTURE TO RESOLVE THE OPEC FISSURE. IT CONSIDERS THE TWO SIDES AS STILL TOO FAR APART TO WORK OUT A COMPROMISE. MOREOVER, GIVEN THE SAUDI ATTITUDE, IT IS THOUGHT THAT THE DYNAMICS OF THE OIL MARKET MAY BE LEFT TO WORK OUT THE PROBLEM. AS MUCH AS IT WOULD LIKE TO SEE A COMPROMISE ON PRICE,
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SHELL IS NOT INDULGING IN "WISHFUL THINKING." SHELL ALSO DOES NOT BELIEVE THAT TOPPING UP OF STOCKS IN LATE 1976 WAS AS GREAT AS TALKED ABOUT BY SOME PEOPLE. IT ESTIMATES THAT THERE IS NO MORE THAN A ONE OR TWO DAY INCREASE IN THE OVERALL STOCKS LEVEL AT YEAREND 1976 AS COMPARED TO THE PREVIOUS YEAR. HENCE, EVEN IF SOME COMPANIES DECIDE TO DRAW DOWN STOCKS FOR A FEW WEEKS TO HOLD OFF BUYING POSSIBLY MORE EXPENSIVE OIL, THERE IS NOT ENOUGH CUSHION. ALTHOUGH SAUDI CONCENTRATION ON HEAVY AND MEDIUM CRUDE PRODUCTION WILL GENERATE SOME PRESSURE ON IRAN AND KUWAIT, IT MIGHT NOT BE ADEQUATE TO SERVE ITS PURPOSE, PARTICULARLY IN THE FACE OF INCREASING MARKET DEMAND.

6. SHELL IS PLEASED TO BE IN LINE TO GET APPROXIMATELY 200,000 B/D (FROM MOBIL) OF THE INCREMENTAL SAUDI PRODUCTION, BUT IT IS LESS THAN ECSTATIC ABOUT 8 OR 9 M/B/D GOING TO THE ARAMCO PARTNERS AT A 5 PERCENT CHEAPER PRICE. SHELL ASSUMES BP, CFP AND ENI WILL GET SIMILAR AMOUNTS, AS REPORTED BY PIW, WITH THE TOTAL INCREMENT FOR NON-ARAMCO COMPANIES NOT SURPASSING 1 M/B/D BEFORE THE END OF MARCH. THEREAFTER, SHELL IS UNCERTAIN WHAT TO EXPECT AND CITES THE KEY QUESTION AS BEING WHETHER THE SAUDIS WILL BE INCLINED TO COMPROMISE EARLY ON WITH THE OTHER SIDE, I.E., THE IRANIANS. THIS IS CONSIDERED A DICEY PROPOSITION AT THE MOMENT SINCE TEMPER MUST FIRST BE ALLOWED TO COOL.

7. BP NOTES ITS OWN ATTITUDES AND TRADING PLANS CONTINUE TO BE A REFLECTION OF THE CONFUSED SITUATION THAT REIGNS WITHIN OPEC. BP HAS SPOKEN WITH PETMIN (APPARENTLY WITH NO DISCERNIBLE RESULT) BUT MOSTLY IT HAS BEEN WATCHING SAUDI ACTIONS FROM A DISTANCE. WHILE INFORMAL TALKS HAVE TAKEN PLACE, NO ARAMCO COMPANY (READ TEXACO) HAS YET MADE A FORMAL, STRUCTURED APPROACH ABOUT BP'S REPORTED ENTITLEMENT TO AN INCREMENTAL

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200,000 M/B/D OF INCREASED SAUDI PRODUCTION. BP CONFIRMS THAT IT HAS TOLD THE KUWAITIS THAT FIRST QUARTER LIFTINGS WILL BE DOWN SHARPLY BUT BOTH SIDES HAVE AGREED, ESSENTIALLY FOR REASONS OF LONGER TERM SELF INTEREST, 'NOT TO THROW THE CONTRACT AT EACH OTHER.' ECHOING SHELL, BP SAYS IT HAS NOT RECEIVED ANY INDICATIONS OF IRAQI PRICE-SHAVING THUS FAR.

8. BP NATURALLY IS MOST SERIOUSLY CONCERNED ABOUT ITS

RELATIONSHIP WITH IRAN. SUTCLIFFE IS EXPECTED TO RETURN
SHORTLY FROM TEHRAN WHERE HIS MISSION HAS BEEN TO POSE
BP'S COMMERCIAL DILEMMA AND PICK UP WHATEVER POLITICAL

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ACTION EB-07

INFO OCT-01 ISO-00 IO-13 AF-08 ARA-06 EA-07 EUR-12 NEA-10
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O R 201740Z JAN 77
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INTELLIGENCE HE CAN ABOUT IRANIAN INTENTIONS. BP ACKNOWLEDGES IT PROBABLY IS WILLING TO ABSORB POTENTIALLY SUBSTANTIAL TRADING LOSSES IF THE TWO TIER PRICE ISSUE IS RESOLVED WITHIN A MONTH OR TWO. (NOTE: BP CALCULATES ROUGHLY THAT A 5 PERCENT PRICE DIFFERENTIAL EQUALS 60 CENTS A BARREL WHILE ITS MARGIN IS 22 CENTS IN IRAN (LESS MINOR DEDUCTIONS), 15 CENTS IN KUWAIT AND QATAR, AND LESS THAN 30 CENTS IN ABU DHABI.) ALTHOUGH THERE IS NO CONTRACTUAL COMMITMENT TO LIFT INSOFAR AS THE CONSORTIUM IS CONCERNED, BP BELIEVES IT IS NOT WORTH JEOPARDIZING THE LONG TERM IRANIAN RELATIONSHIP IF THE SAUDI-IRANIAN RIFT IS GOING TO BE BRIDGED EARLY ON. HOWEVER, BP'S BEST GUESS (PENDING SUTCLIFFE'S REPORT FROM IRAN) IS THAT NO COMPROMISE WILL BE REACHED UNTIL THE NEXT OPEC MINISTERIAL IN JULY IS NEAR AT HAND.

9. COMMENT: PRESUMABLY THE IEA COUNTRIES WILL PROCEED UNDER ANY CIRCUMSTANCES TO SHARE INFORMATION ON STOCKS, COMPANY AND PRODUCER INTENTIONS, ETC. THAT BEARS ON THE TWO TIER PRICING SITUATION. IT IS DIFFICULT TO ENVISAGE HOWEVER REACHING AGREEMENT EVEN ON LIMITED SUPPORTIVE MEASURES SUCH AS GOVERNMENTAL WILLINGNESS TO JAWBONE OR OTHERWISE ENCOURAGE OIL COMPANIES TO COOPERATE WITH THE SAUDI/UAE CAMPAIGN UNLESS WE CAN BRING THE BRITISH (AND LIKE-MINDED EUROPEANS) ALONG ON THE KEY ASPECTS OF OUR ANALYSIS OF FUTURE OIL MARKET DEMAND AND SAUDI PRODUCTION CAPABILITY AND INTENTIONS, FOR EXAMPLE. TO AVOID THE PROSPECT OF US AND UK POLICY HEADING IN OPPOSITE DIRECTIONS BASED ON DIAMETRICALLY OPPOSED ANALYSES, WE SUGGEST THAT CONSIDERATION BE GIVEN TO HOLDING HIGH LEVEL US-UK BILATERAL TALKS TO CLARIFY POINTS OF DISAGREEMENT OR MISUNDERSTANDING. FURTHER, CONFIDENTIAL

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WE MIGHT SEEK TO EXPEDITE THE TRANSFER AND PERHAPS INCREASE THE QUANTITIES OF INCREMENTAL SAUDI/UAE CRUDE MADE AVAILABLE TO SHELL, BP, CFP AND ENI FROM THE ARAMCO PARTNERS.

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Message Attributes

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